

MEMORANDUM

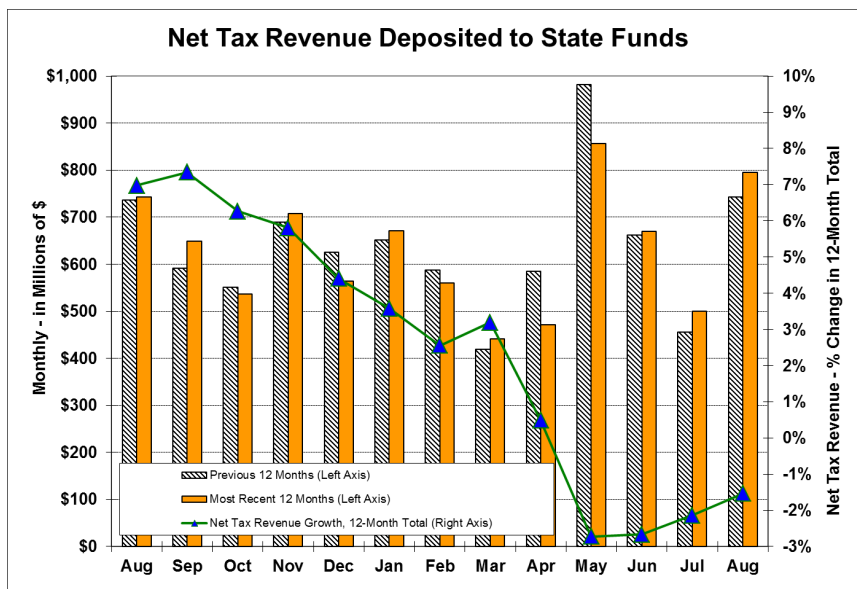
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: September 22, 2014

Twelve-month Total Net Tax Receipts Through August 31, 2014

The attached spreadsheet presents net tax revenue deposited to State funds for the 12-month period ending August 2014 with comparisons to the previous 12 months. August 2013 to August 2014 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



Overview of Current Situation

Annual State tax receipts, net of tax refunds, turned negative in May 2014 and year-over-year annual growth is now negative 1.5%. Although much of the reversal can be traced to individual income tax changes at the State and federal level, banking, corporate, gambling, and real estate transfer taxes are also negative over the most recent 12 months. Iowa's nonfarm employment growth stands at 1.6% (12-month average) and income tax withholding as well as sales/use tax deposits are now showing good growth, indicating that the Iowa economy continues to expand.

Month of August 2014

August net tax receipts totaled \$795.7 million, an increase of \$52.6 million (7.1%) compared to August 2013. Individual income tax withholding and sales/use tax provided the increase for August. Cigarette/tobacco, corporate, and fuel taxes each declined.

Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending August 2014, net revenue from all taxes deposited to State funds totaled \$7.422 billion, a decrease of \$116.0 million (- 1.5%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$224.9 million, - 6.5%) – Annual individual income tax revenue growth peaked at \$451.4 million for the 12 months ending June 2013. Due to an increase in the Iowa Earned Income Tax Credit, the new Taxpayer Trust Fund Tax Credit, and the FY 2013 one-time boost to revenue that was the result of federal tax changes enacted January 1, 2013, the annual rate of income tax revenue growth declined significantly, falling below 0.0% by May 2014. The most recent three months have each shown improvement.
- Sales/Use Tax (positive \$151.3 million, 6.3%) – For the forty-eighth consecutive month, the annual growth in sales/use tax deposits has been positive.
- Corporate Income Tax (negative \$33.0 million, - 7.7%) – Corporate income tax has been volatile in recent months and has trended lower over the past two years.
- Bank Tax (negative \$8.4 million, - 21.6%) – The use of income tax credits may explain the recent weakness in bank (franchise) tax receipts. Banks utilize income tax credits and often those credits are purchased from other taxpayers with insufficient tax liability to use the credits themselves.
- Fuel Tax (positive \$8.9 million, 2.0%) – According to Department of Revenue monthly fuel sales reports, over the most recent 12-month period, Iowa taxable gasoline/ethanol gallons sold increased 3.7%. Taxable diesel sales increased 5.8%. The annual total for all taxable fuel gallons sold in Iowa is currently 0.3% below the last peak (12 months ending July 2011).
- Gambling Tax (negative \$9.9 million, - 3.3%) – According to Racing and Gaming Commission statistics, 13 of Iowa's 18 casino/track locations recorded negative annual adjusted gross revenue (AGR) growth for the 12 months ending August 2014. The combined AGR change for the 18 facilities was negative 3.1% over the previous 12 months. Across all facilities, the AGR for the most recent 12 months totaled \$1.392 billion. The annual AGR total has been declining and is 5.3% below the November 2012 peak.
- Real Estate Transfer Tax (negative \$1.8 million, - 9.2%) - Real estate transfer tax deposits, an indicator of real estate sales statewide, have declined over the past three months.
- Cigarette and Tobacco Tax (negative \$3.2 million, - 1.4%)

Tax Spotlight – Corporate Income Tax

Corporate income is taxed under the authority of [Iowa Code Chapter 422](#), Division III. The tax is imposed on the net income of corporations doing business in Iowa or receiving income from property located in Iowa. Taxation of corporate income by the State of Iowa is based on the share of total company sales occurring within Iowa (single factor formula). Corporate income tax rates are applied as follows:

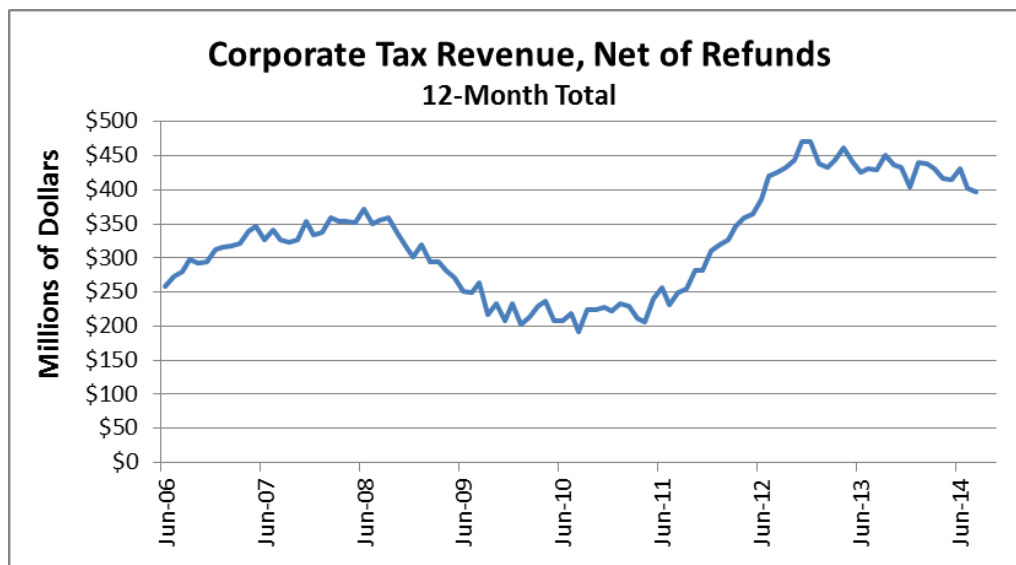
- 6.0% on the first \$25,000 of net income

- 8.0% on the next \$75,000
- 10.0% on the next \$150,000
- 12.0% on amounts in excess of \$250,000

An alternative minimum tax may be imposed at an effective rate of 7.2% if it exceeds the corporation's regular tax liability. Iowa is similar to most states using the federal corporate taxable income of a corporation as the basis for Iowa corporate income tax. Iowa allows for the deduction of 50.0% of federal corporate income tax paid prior to calculating State corporate income tax liability.

The Iowa corporate income tax was first imposed in 1934 at a single rate of 2.0% with the passage of HF 1 (Income, Corporation, and Sales Tax Act). The rate remained at 2.0% until 1955 when it was increased to 3.0%, decreased to 2.0% in 1957, increased again to 3.0% in 1959, and increased to 4.0% in 1965. With the passage of HF 702 in 1967, the corporate income tax rate was changed from a single rate to varying rates at different income levels starting at 4.0% on the first \$25,000, 6.0% on the next \$75,000, and 8.0% for amounts in excess of \$100,000. In 1971, HF 654 increased the rates 2.0 percentage points (6.0%, 8.0%, and 10.0%). The current corporate income tax rates and income levels were approved in HF 2171 (Taxation Act of 1982).

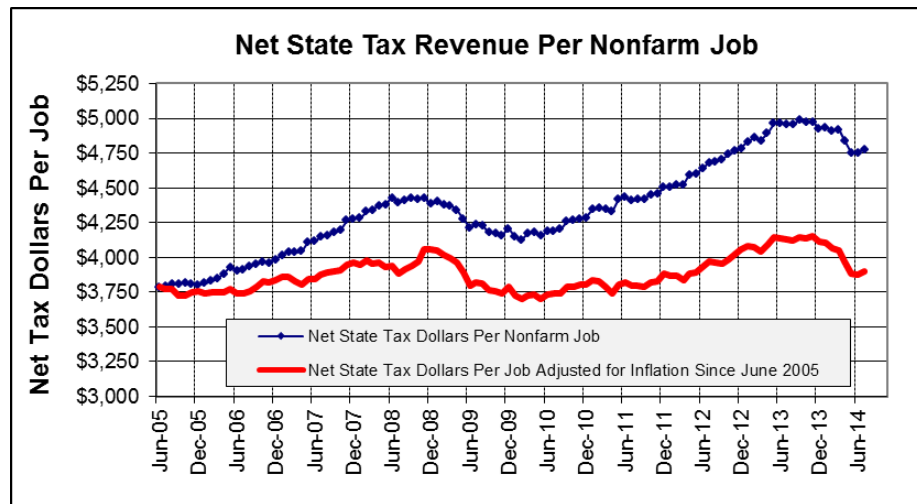
Corporate income tax returns are filed by the last day of the fourth month following the end of the corporation's tax year. Cooperatives (as defined by the Internal Revenue Code) are to file a return by the 15th of the ninth month after the end of the cooperative's tax year. Nonprofit corporation returns are due by the 15th of the fifth month after the end of the nonprofit corporation's tax year. Most corporations are required to make estimated tax payments quarterly. All corporate income tax revenues are deposited in the State General Fund.



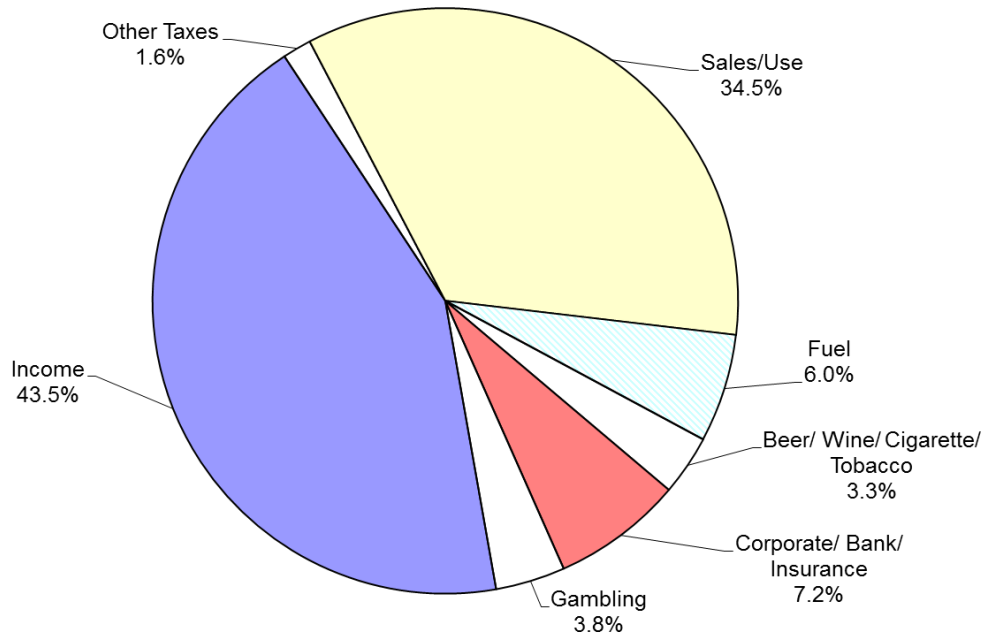
Tax Revenue and Employment

The average reading for Iowa nonfarm employment over the 12 months ending July 2014 is 1,542,700 and net State tax receipts over the same 12 months totaled \$7.369 billion, or \$4,777 per nonfarm job. This is \$992 higher than the per-job average for the 12 months ending June

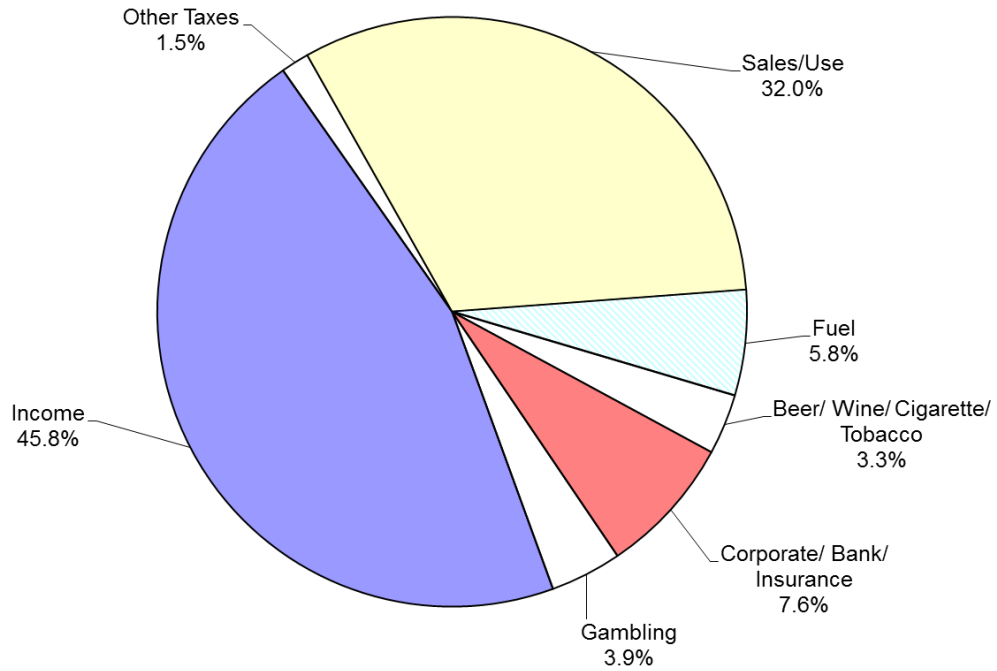
2005. The blue line on the following chart depicts the annual tax revenue collected by the State per job, calculated monthly. The red line subtracts the impact of inflation since June 2005 from the blue line. The red line indicates that inflation adjusted tax revenue per job has increased \$115 since June 2005 and the remainder of the \$992 increase (\$877) represents the impact of inflation.



Net State Tax Revenue - Twelve Months Ending August 2014
Net Revenue = \$7.422 Billion
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending August 2013
Net Revenue = \$7.538 Billion
Percentages may not add to 100% due to rounding



Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of August 2013	Month of August 2014	August \$ Change	August % Change
Banking	\$ 38.8	\$ 30.4	\$ - 8.4	-21.6%	\$ 0.0	\$ 2.5	\$ 2.5	--
Beer & Wine	22.0	22.0	0.0	0.0%	2.0	2.1	0.1	5.0%
Cigarette & Tobacco	227.8	224.6	- 3.2	-1.4%	22.5	19.7	- 2.8	-12.4%
Corporate Income	429.3	396.3	- 33.0	-7.7%	10.0	3.2	- 6.8	-68.0%
Fuel	435.4	444.3	8.9	2.0%	33.8	28.0	- 5.8	-17.2%
Gambling	295.6	285.7	- 9.9	-3.3%	26.1	25.8	- 0.3	-1.1%
Individual Income	3,454.4	3,229.5	- 224.9	-6.5%	294.2	328.6	34.4	11.7%
Inheritance	85.3	88.9	3.6	4.2%	6.3	9.2	2.9	46.0%
Insurance	106.6	107.9	1.3	1.2%	48.3	50.4	2.1	4.3%
Other Taxes	11.9	12.0	0.1	0.8%	2.0	1.8	- 0.2	-10.0%
Real Estate Transfer	19.5	17.7	- 1.8	-9.2%	1.8	0.8	- 1.0	-55.6%
Sales/Use	2,411.2	2,562.5	151.3	6.3%	296.1	323.6	27.5	9.3%
Total Net Taxes	\$ 7,537.8	\$ 7,421.8	\$ - 116.0	-1.5%	\$ 743.1	\$ 795.7	\$ 52.6	7.1%
Gross Tax & Refunds								
Gross Tax	\$ 8,846.7	\$ 8,851.3	\$ 4.6	0.1%	\$ 811.9	\$ 861.5	\$ 49.6	6.1%
Tax Refunds	\$ - 1,309.1	\$ - 1,429.5	\$ - 120.4	9.2%	\$ - 68.8	\$ - 65.9	\$ 2.9	-4.2%
Net Tax Receipts by Fund								
State General Fund (GF)	\$ 6,388.0	\$ 6,100.1	\$ - 287.9	-4.5%	\$ 626.3	\$ 685.5	\$ 59.2	9.5%
Road Use Tax Fund	\$ 764.7	\$ 786.2	\$ 21.5	2.8%	\$ 66.5	\$ 62.2	\$ - 4.3	-6.5%
Non-GF Gambling	\$ 252.8	\$ 284.0	\$ 31.2	12.3%	\$ 25.9	\$ 25.6	\$ - 0.3	-1.2%
Other State Funds	\$ 132.0	\$ 251.4	\$ 119.4	90.5%	\$ 24.5	\$ 22.3	\$ - 2.2	-9.0%
Local Option Taxes *	\$ 893.2	\$ 871.4	\$ - 21.8	-2.4%	\$ 75.8	\$ 77.0	\$ 1.2	1.6%

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

A percentage change displayed as "--" represents instances where the base year net revenue amount was zero or negative so no meaningful percentage change can be calculated.

Tax Categories Used in Table

Franchise (Bank) Tax: The franchise tax paid by banks is deposited in the State General Fund. Credit unions are taxed under a different system than banks, but the credit union tax is included in this line also. Of the total deposited, the bank tax provides approximately 98.0% of the revenue and the credit union tax 2.0%.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited in the State General Fund, the Liquor Control Fund, and a small amount is deposited in an Iowa Economic Development Authority fund for wine promotion.

Cigarette & Tobacco Tax: Prior to July 1, 2011, all cigarette and tobacco products tax revenue was deposited to the State General Fund. Beginning FY 2012, the first \$106.0 million of revenue from cigarette and tobacco taxes is deposited to the Health Care Trust Fund and the remainder is deposited to the State General Fund. Beginning FY 2014, all cigarette and tobacco tax revenue is deposited to the Health Care Trust Fund.

Corporate Income Tax: All corporate income tax is deposited in the State General Fund.

Motor Vehicle Fuel Tax: All motor vehicle fuel tax is deposited in one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: Gambling tax is deposited in several State funds. For FY 2013, \$40.0 million was deposited to the General Fund and the remainder to other State funds. Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, the County Endowment Fund, the Vision Iowa Fund, the Revenue Bond Debt and Subsidy Holdback Funds, the Technology Reinvestment Fund, and the Iowa Skilled Worker and Job Creation Fund.

Individual Income Tax: Most individual income tax revenue is deposited in the State General Fund. A total of \$4.0 million per year is deposited in the Workforce Development Fund. An annual \$2.6 million diversion to the Child Daycare Fund ended in FY 2009. In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited in a State fund. That revenue is not included here.

Inheritance Tax: All inheritance tax is deposited in the State General Fund.

Insurance Premium Tax: All insurance premium tax is deposited in the State General Fund.

Other Taxes: Other taxes include brucellosis eradication property tax (deposited in a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

Real Estate Transfer Tax: Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The distribution of State portion of real estate transfer tax revenue is currently changing each fiscal year, with the State General Fund portion reduced to 65.0% by FY 2015. The portion not deposited to the State General Fund is deposited to the Housing Trust Fund and the Shelter Assistance Fund.

Sales/Use Tax: General sales/use tax is deposited in the State General Fund, while most vehicle use tax is deposited in the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax is referred to as a fee in the Iowa Code. To allow continuity of data, the revenue from the fee is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted from State revenue as part of the net sales/use tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Beginning FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

Report Database: The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.